

Ms. Ann E. Misback  
Secretary  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> St & Constitution Ave NW  
Washington, DC 20551

August 17, 2021

Re: Docket No. R-1748, RIN 7100-AG15; Debit Card Interchange Fees and Routing

Dear Ms. Misback:

On behalf of the Employers Council on Flexible Compensation (“ECFC”), we are submitting this letter in response to the request from the Board of Governors of the Federal Reserve System (the “Board”) for comment on its notice of proposed rulemaking to amend Regulation II and the Official Board Commentary (“Commentary”) on Regulation II to clarify Regulation II requirements related to the prohibition on network exclusivity and standardize certain terminology (the “Proposal”). ECFC is grateful for the opportunity to comment on this Proposal.

ECFC is a membership association dedicated to preserving and expanding employer-provided tax-advantaged benefit choices for working Americans, including account-based plans which provide benefits in areas such as health care, childcare, and commuting. These benefits provide families with the support they need to meet their everyday living expenses and remain productive members of the workforce. ECFC’s members include employers and companies who provide administrative and consulting services to employer sponsors of employee benefit plans, including health savings accounts, health flexible spending arrangements, dependent care assistance flexible spending arrangements, and health reimbursement arrangements, commuter and parking benefits, and COBRA continuation coverage. ECFC member companies assist in the administration of cafeteria plan and health benefits for over 33 million employees.

As discussed more fully herein, an important aspect of benefit plan administration is the ability to administer and adjudicate certain health and dependent care claims electronically with electronic payment cards as required by Internal Revenue Service (“IRS”) guidance. ECFC understands the Proposal is intended to clarify obligations and is “not intended to impose new obligations with respect to card-not-present transactions,” but ECFC believes aspects of the Proposal seem to be inconsistent with Section 1075 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Act”), in that the effect of the Proposal would be to prescribe requirements beyond those necessary to ensure the availability of two unaffiliated networks. The Proposal is also a considerable modification of industry practices that could have a particularly significant impact on the operation and structure of flexible spending accounts (“FSAs”), health reimbursement arrangements (“HRAs”) and health savings accounts (“HSAs”) that employ health benefit card technology (together, “Health Benefit Cards”) insofar as the Board’s Proposal will effectively make Health Benefit Card issuers responsible for ensuring there is network choice for covered health care-related debit transactions despite the lack of auto-transaction validation infrastructure in place to support multiple networks today. Ultimately we

are concerned that if the Board finalizes its Proposal as proposed, the availability of and benefits provided by Health Benefit Cards will be substantially reduced in light of the new substantive obligations that will be placed on issuers, merchants, and the ECFC member companies that support Health Benefit Card programs, to the detriment of employers and consumer cardholders that rely on these programs. Moreover, utilization of Health Benefit Cards has greatly increased the popularity (and availability) of FSAs, HRAs, and HSAs as consumer-oriented benefits among employer plan sponsors. Restricting Health Benefit Card availability could result in important benefit plans being curtailed or eliminated by their employer plan sponsors.

## **I. Background**

### **a. Current Rule**

In June 2011, the Board issued a final rule, Regulation II, implementing Section 1075 of the Act. Section 1075 of the Act amended the Electronic Fund Transfer Act<sup>1</sup> and required the Board to develop rules that prohibit payment card networks and issuers from: (1) restricting the payment card networks on which an electronic debit transaction may be processed to a single payment card network or affiliated group of payment card networks (the “Network Exclusivity Prohibition”); and (2) inhibiting the right of a person accepting or honoring debit cards to route an electronic debit transaction over any payment card network that is enabled to process such transaction (the “Routing Restriction Prohibition”).

Section 235.7(a) of Regulation II implements the Network Exclusivity Prohibition, which prohibits an issuer or payment card network from “restrict[ing] the number of payment card networks on which an electronic debit transaction may be processed to less than two unaffiliated networks.”<sup>2</sup> The current law specifies an issuer can comply with this requirement by allowing “an electronic debit transaction to be processed on at least two unaffiliated payment card networks, each of which does not, by rule or policy, restrict the operation of the network to a limited geographic area, specific merchant, or particular type of merchant or transaction, and each of which has taken steps reasonably designed to enable the network to process the electronic debit transactions that the network would reasonably expect will be routed to it.”<sup>3</sup>

Section 235.7(b) of Regulation II implements the Routing Restriction Prohibition, which restricts any issuer or payment card network from “inhibit[ing] the ability of any person that accepts or honors debit cards for payments to direct the routing of electronic debit transactions for processing over any payment card network that may process such transactions.”<sup>4</sup>

### **b. Proposal**

ECFC believes the provisions of the Proposal described in this section are those that could most significantly impact Health Benefit Cards. Section 235.7(a)(2) would be amended to provide that an issuer satisfies the requirements of the Network Exclusivity Prohibition “only if, for every geographic area, specific merchant, particular type of merchant, and particular type of transaction for which the issuer’s debit card can be used to process an electronic debit

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<sup>1</sup> 15 U.S.C. § 1693 et seq.

<sup>2</sup> 12 C.F.R. § 235.7(a)(1).

<sup>3</sup> 12 C.F.R. § 235.7(a)(2).

<sup>4</sup> 12 C.F.R. pt. 235, app. A, at 7(a)-2.



transaction, such issuer enables at least two unaffiliated payment card networks to process an electronic debit transaction, and where each of these networks has taken steps reasonably designed to be able to process the electronic debit transactions that it would reasonably expect will be routed to it, based on expected transaction volume.”<sup>5</sup>

The Proposal also amends related Commentary to the Network Exclusivity Prohibition. Comment 7(a)-1 would reflect that Section 235.7(a) “requires an issuer to configure each of its debit cards so that each electronic debit transaction initiated with such card can be processed on at least two unaffiliated payment card networks . . . for every geographic area, specific merchant, particular type of merchant, and particular type of transaction for which the issuer’s debit card can be used to process an electronic debit transaction.”<sup>6</sup> So long as this condition is satisfied, an issuer would not need to configure its debit cards in this manner for each method of cardholder authentication currently in existence or that may be developed in the future.

Comment 7(a)-2 would provide “[a] payment card network could be used to satisfy the requirement that an issuer enable two unaffiliated payment card networks for each electronic debit transaction if the network was either (a) capable of processing the volume of electronic debit transactions that it would reasonably expect to be routed to it or (b) willing to expand its capabilities to meet such expected transaction volume.”<sup>7</sup> The Board would clarify that a payment card network would not qualify for purposes of satisfying the Network Exclusivity Prohibition if “the network’s policy or practice is to limit such expansion.”<sup>8</sup>

Comment 7(a)-2.iii would provide that an issuer must enable at least two unaffiliated payment card networks “[f]or every geographic area (e.g., New York), specific merchant (e.g., specific fast food restaurant chain), particular type of merchant (e.g., fast food restaurants), and particular type of transaction (e.g., card-not-present transaction) for which the issuer’s debit card can be used to process an electronic debit transaction . . . .”<sup>9</sup> Comment 7(a)-2.iii would illustrate how an issuer could comply with the requirement to enable at least two unaffiliated payment card networks for every geographic area and for every particular type of transaction.<sup>10</sup>

## II. Special Considerations for Health Benefit Cards

Health Benefit Cards differ from traditional debit cards in that IRS regulations require Health Benefit Cards to use health expense adjudication technology. Health Benefit Cards are limited in use to (1) medical care providers (as identified by certain health care merchant category codes), (2) merchants where 90% of a location’s gross receipts from the prior year consist of items that qualify as medical expenses according to the IRS, and (3) merchant locations using an Inventory Information Approval System (“IIAS”) that meets the IRS’s requirements.

An IIAS is a system that uses inventory information (e.g., stock-keeping units) to compare items purchased by a cardholder against a pre-established list of eligible health care expenses set forth in the Internal Revenue Code. The system only approves the use of the card for eligible

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<sup>5</sup> 86 Fed. Reg. 26189, 26194.

<sup>6</sup> *Id.*

<sup>7</sup> 86 Fed. Reg. 26189, 26194.

<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*

health care expenses. An IIAS allows cardholders to purchase eligible health care items at the point-of-sale without further substantiation. For example, a cardholder participating in her employer's health FSA with a card program could use her FSA card at a grocery store to purchase \$20 of eligible health care items and \$20 of groceries. The IIAS would only approve the use of her FSA card to purchase the eligible health care items. The cardholder would then have to use another payment method for her groceries.

The IRS requires an IIAS to be in place at merchants to ensure Health Benefit Cards are used only for eligible expenses and to ensure certain recordkeeping requirements are met. Health expense auto-adjudication technology, such as the IIAS standard that is maintained by the Special Interest Group for IIAS Standards ("SIGIS"), is not currently generally supported by all payment card networks. Five PIN debit and three signature payment card networks that have certified their compliance with SIGIS.<sup>11</sup> Those eight networks are owned by four payment card brands or processors and represent some of the largest networks with wide acceptance in the merchant community. In addition, in order to participate in an IIAS arrangement, a merchant must also undertake the certification process and administrative work associated with conducting an inventory of its goods to support an IIAS certification and then choose to route the transactions to other networks.

The process to implement transactions on the IIAS network requires development by the merchants to provide the data required for automatic authentication. Following such development, merchants must certify with SIGIS. Over 13,000 merchants have undertaken the development and certified with SIGIS for signature transactions, representing a very broad acceptance footprint for Health Benefit Cards. On the other hand, to date, only one merchant has chosen to complete the required development and certification work to support the standard for PIN transactions. Today, in the Health Benefit Card space, merchants have the choice where to route transactions and they are choosing not to route transactions to PIN debit networks - either by failing to acquire point-of-sale PIN terminals and devices or by not investing and certifying the technology necessary to route such transactions. Health Benefit Cards are already enabled for two unaffiliated networks that support SIGIS IIAS for PIN transactions, and the Proposal would extend beyond the requirement in the Act to enable two unaffiliated networks by making the issuers and networks responsible for merchant inactivity. Moreover, even if the Proposal is finalized, we do not see the Proposal changing merchant activity in any meaningful way, and without merchant adoption of IIAS for PIN transactions it would be impossible for issuers to comply, notwithstanding their enablement of their cards to support two unaffiliated networks.

If a merchant uses a payment card network that is not SIGIS certified for a purchase made with a Health Benefit Card, the transaction will fail. If a Health Benefit Card transaction is declined, the cardholder will need to pay with another method of payment and submit a claim form with their itemized receipt to their Health Benefit Card Administrator for reimbursement. Filing separate claims is a significant inconvenience for the cardholder and could impact the use of the cardholder's health care benefits. It is estimated that workers already forfeit between \$400 million to \$500 million annually in unspent FSA funds.<sup>12</sup> Health Benefit Cards are an important

<sup>11</sup> The Special Interest Group for IIAS Standards, *SIGIS Member Networks*, available at: <https://sig-is.org/publications/sigis-member-networks>.

<sup>12</sup> Darla Mercado, *You Only Have a Few Weeks to Spend Down These Tax-Advantaged Dollars*, CNBC, available at: <https://www.cnbc.com/2020/11/25/you-only-have-a-few-weeks-to-spend-down-these-tax-advantaged-dollars.html>.



means of access to consumer funds as they make it easier and faster for cardholders to access and use their funds.

### III. ECFC's Comments on the Proposal

ECFC appreciates the opportunity to comment on the Proposal and raise its concerns with the Board regarding how the Proposal may have unintended consequences for employer plans that offer Health Benefit Cards and, most importantly, for the employee cardholders and their families who use Health Benefit Cards.

a. The Proposal may create an unworkable standard for issuers to meet, which could ultimately result in issuers greatly reducing or discontinuing their offerings of Health Benefit Cards. ECFC requests the Board eliminate the requirement that an issuer satisfy the Network Exclusivity Prohibition with respect to every "specific merchant" and every "particular type of merchant."

#### *1. There is ambiguity surrounding what it means to be a "particular type of merchant."*

The Proposal requires an issuer to ensure "at least two unaffiliated payment card networks" have been enabled with respect to every "specific merchant" and every "particular type of merchant." As an initial matter, these terms are not all clearly defined in the Proposal. As discussed below, issuers can enable cards consistent with the Proposal, but only merchants can "ensure" that the alternate networks are actually made available either at point of sale or on-line.

The Board's edits to the Commentary provide some clarity regarding the term "specific merchant," but ambiguity remains regarding the definition of "particular type of merchant." Comment 7(a)-2.iii suggests "'particular type of merchant" refers to a category of merchants (e.g., fast food restaurants), but it is unclear how such merchant categories would be determined. In particular, it is unclear whether such categories would be based on payment card network merchant category codes.

Merchant category codes ("MCCs") are critical in determining whether a customer can use a Health Benefit Card in order to pay for health care expenses. Only a limited set of health care related MCCs are automatically enabled to accept Health Benefit Cards. Merchants outside of these MCCs must affirmatively route transactions on IIAS-certified networks. Because a significant amount of health benefit purchases occur at non-health care MCC merchants, ongoing availability of IIAS transactions is critical.

#### *2. Issuers could be liable for actions or inactions of payment card networks, merchants, and third-party service providers.*

In the release accompanying the Proposal, the Board stated "[t]he network used to process a transaction depends primarily on the set of networks that the issuer has enabled for the transaction and the specific network that the merchant or its acquirer chooses to route the transaction out of those available," but also acknowledged other factors, "such as whether the merchant can support the authentication methods used by the available networks. It may also

depend on the cardholder's choice of authentication method in situations where the merchant has configured its card terminal to enable cardholder choice.”<sup>13</sup>

Merchants and their third party service providers generally control which payment card network cards they will accept. Issuers do not typically have control or insight into this decision. Accordingly, an issuer that enables two payment card networks on its debit cards to satisfy the Network Exclusivity Provision may no longer be compliant with the Proposal if a merchant or its third party service provider does not accept one of the payment card networks that the issuer has initially enabled, or decides to cease continue accepting debit cards issued on one of those payment card networks. Compliance with this provision of the Proposal would, at the very least, result in a considerable initial and ongoing operational burden and expense on all issuers, but ultimately, since network routing is at the merchant's choice, it will be impracticable, if not impossible, for an issuer to comply with the Proposal for every “specific merchant” and “particular type of merchant.”

### *3. Issuers and employers may be less inclined to offer their Health Benefit Cards.*

Currently, there are only a small handful of issuers of Health Benefit Cards in the marketplace. The potential for increased liability for issuers coupled with the unworkable standard of ensuring at least two unaffiliated payment card networks capable of processing Health Benefit Card transactions for every merchant and every transaction type in every geographic area for which a Health Benefit Card can be used under the Proposal may result in issuers reducing or even discontinuing their Health Benefit Card programs altogether. This could ultimately result in reduced competition in the space to the detriment of employers and consumer cardholders. Moreover, utilization of Health Benefit Cards has greatly increased the popularity (and availability) of these types of consumer oriented benefits among employer plan sponsors. Restricting Health Benefit Card availability would result in such important benefit plan being curtailed or eliminated.

#### b. The Proposal may result in significant inconvenience for cardholders and added costs for employer administrators in the form of manual claim processing.

Health Benefit Cards lower employers' benefit administration costs through the auto-adjudication features and offer cardholders immediate and convenient access to their benefit dollars. One of the benefits of the IAS standard is it enables cardholders to purchase small, eligible medical expense items from merchants they already visit.

Due to IRS requirements, an attempt by all but one merchant to route a Health Benefit Card transaction on a PIN network (even one that is SIGIS certified) will fail because no other merchants have certified for SIGIS IAS on a PIN network. Cardholders will therefore not be able to use their Health Benefit Cards to make such purchases. Instead, cardholders would have to submit documentation substantiating their purchases and await reimbursement. ECFC is concerned that in the event the Proposal impacts issuance and availability of Health Benefit Cards, the convenience of auto-adjudication, in particular for small medical expenses, will be less available to cardholders. This could result in fewer cardholders using their health care benefits. Without auto-adjudication, administration costs for the health benefits will likely

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<sup>13</sup> 86 Fed. Reg. 26189, 26190 n. 11.



increase as claims will need to be processed manually. Moreover, a contraction or elimination of IIAS enabled merchants would result in a significant increase in the cost associated with administering Health Benefit Card claims and could potentially result in an elimination of such programs altogether.

c. The Proposal is unlikely to result in a benefit to cardholders with Health Benefit Cards.

The Board noted in its press release that “[t]he absence of at least two unaffiliated networks for card-not-present transactions forecloses the ability of merchants to choose between competing networks when routing such transactions, an issue that has become increasingly pronounced because of continued growth in online transactions, particularly in the COVID-19 environment.”<sup>14</sup> The Board’s concern seems to be that merchants are being unfairly restricted from routing transactions to unaffiliated networks in an online environment.

In the final rule announced by the Board in 2011, the Board highlighted that the savings to merchants “could potentially be passed on to consumers as lower retail prices.”<sup>15</sup> In the event the Board believes potential savings to merchants resulting from the Proposal would be passed on to cardholders, ECFC believes the potential savings passed along by merchants with regard to Health Benefit Cards would be non-existent or insignificant. Purchases by such cards make up a small fraction of total health care purchases, and any impact with respect to such Health Benefit Cards would be immaterial.

To the contrary, as noted above, final adoption of the Proposal could lead to a restriction in or elimination of the availability of and ability to use Health Benefit Cards. This would negatively impact the millions of consumers who today enjoy the flexibility and convenience of being able to immediately access the funds in their benefit accounts without the need to submit a claim and pay for their healthcare expenses with other household funds while waiting for reimbursement.

d. ECFC requests that the Board consider the unique aspects of Health Benefit Cards that support electronic adjudication.

The Board previously acknowledged the challenges created by the application of the Network Exclusivity Prohibition to Health Benefit Cards by granting a delayed effective date for issuer compliance. Unfortunately, there remain similar challenges with the Proposal. Accordingly, ECFC requests the Board reconsider its proposed approach.

As the Board continues to consider commentary and examine related data, ECFC encourages the Board to engage in discussion with ECFC and other industry participants before undertaking further administrative action regarding Regulation II.

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<sup>14</sup> See Federal Reserve System, Press Release, Federal Reserve Board invites public comment on proposed changes to Regulation II regarding network availability for card-not-present debit card transactions and publishes a biennial report containing summary information on debit card transactions in 2019, available at:

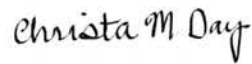
<https://www.federalreserve.gov/newsevents/pressreleases/bcreg20210507a.htm> (May 7, 2021).

<sup>15</sup> Debit Card Interchange Fees and Routing, 76 Fed. Reg. 43394, 43420 (July 20, 2011).

Thank you for your consideration and review of this letter. If you have any questions or wish to discuss the content of this letter further, please do not hesitate to contact Christa Day (202-659-4300 or [cday@ecfc.org](mailto:cday@ecfc.org)) or Bill Sweetnam (202-465-6397 or [wsweetnam@ecfc.org](mailto:wsweetnam@ecfc.org)).

Sincerely,

Christa M. Day  
Executive Director



William F. Sweetnam, Jr.  
Legislative and Technical Director

